

VZCZCXRO9683
PP RUEHCI
DE RUEHKT #2195/01 2261223
ZNR UUUUU ZZH
P 141223Z AUG 06
FM AMEMBASSY KATHMANDU
TO RUEHC/SECSTATE WASHDC PRIORITY 2745
INFO RUEHBK/AMEMBASSY BANGKOK PRIORITY 6109
RUEHHE/AMEMBASSY HELSINKI PRIORITY 0106
RUEHNE/AMEMBASSY NEW DELHI PRIORITY 0098
RUEHTL/AMEMBASSY TALLINN PRIORITY 0005
RUEHUM/AMEMBASSY ULAANBAATAR PRIORITY 0026
RUEHCI/AMCONSUL CALCUTTA PRIORITY 2801

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E.O. 12958: N/A

TAGS: [OREP](#) [AMGT](#) [ASEC](#) [AFIN](#) [NP](#)

SUBJECT: NEPAL SCENESETTER FOR AUGUST 25-28 VISIT OF CODEL
KOLBE

REF: STATE 116910

SUMMARY AND INTRODUCTION

11. Your visit comes at a critical moment in Nepal's history.

Many in the country hope that Nepal is perhaps closer to establishing lasting peace than it has been at any other time during the 10-year-old Maoist insurgency. On August 9, the Nepalese Prime Minister GP Koirala and the Maoist leader Prachanda signed identical letters to UN Secretary General Kofi Annan requesting a greatly enlarged UN role, notably including monitoring of the Maoist combatants. The letters, however, did not address the central issue of separating the Maoist from their weapons. Meanwhile, drafters have nearly completed an interim constitution which could lead to an interim government with Maoist participation and elections for a constituent assembly perhaps as soon as April 2007. The government continues to insist, however, that the Maoists will not be allowed to enter the government until they are separated from their weapons. The nationwide elections would be the first in nearly a decade. The coalition government is struggling to deal with multiple challenges, including an ailing Prime Minister, the difficulties of maintaining internal cohesion within a seven-party coalition, continued Maoist violence, limited financial resources and a battered economy.

12. Your trip comes on the heels of a very successful visit August 12-14 of Senator Arlen Specter. Your visit will bolster a friendly democratic government that is badly in need of U.S. support. End Summary and Introduction.

THE SPA AND THE MAOISTS RULE THE SCENE

13. The Seven-Party Alliance (SPA) and the Maoists have dominated the political scene since King Gyanendra reinstated Parliament on April 24. Since then, the King has largely disappeared from the public eye. The SPA - a coalition of political parties that opposed the King's February 2005 takeover - and the Maoists have had great difficulty transforming the alliance they formed against the King's dictatorship into an agreement on a working system of government. While demanding a share of power in Kathmandu, the Maoists refuse to abandon their campaign of violence. In the meantime, the SPA has been hard pressed to merge the diverse views of its member parties into a common voice. It also faces challenges because of repeated hospitalizations of Prime Minister and center-right Nepali Congress (NC) President GP Koirala. No other party leader in any party commands the same nationwide standing and it is unclear who could or would succeed him.

CAREENING TOWARD DEMOCRACY

¶4. The April pro-democracy movement and the reinstatement of the 205-plus-member House of Representatives, the lower house of Parliament, led to a dizzying pace of transformation. MPs returned to the seats they last held in 2002 and agreed to work toward constituent assembly elections. During the following month, the House of Representatives issued decrees that limited the powers of the King and declared Nepal a secular state. The House also stripped the Nepal Army of the "Royal" moniker and placed it under parliamentary control. The GON and Maoists created negotiation teams to lead the peace process dialogue. On May 26, the GON and Maoists signed a 25-point Code of Conduct to govern each side's unilateral cease-fire.

A PEACE PROCESS ON TWO LEVELS

¶5. The GON and Maoist negotiation teams planned high-level "summit" meetings to work through the formal peace process, but many decisions have sprung from informal meetings between Maoist and SPA leaders. Tensions have arisen between the two largest SPA parties, the NC and the Communist Party of Nepal-United Marxist Leninist (CPN-UML -- the largest center-left party), and the other SPA parties because the other parties feel excluded from decisionmaking. PM Koirala has also faced public criticism for allegedly conducting private negotiations with the Maoists. These private talks led in mid-June to an eight-point agreement that was widely criticized by SPA members. That document did, however, lead

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to the creation of the Interim Constitution Drafting Committee and the National Monitoring Committee for the Cease-fire Code of Conduct.

ALL EYES ON ARMS MANAGEMENT

¶6. Management of the Maoist arms, specifically separation of the Maoist combatants from their arms, remains perhaps the primary issue in the peace process. The identical letters to the Secretary General PM Koirala and Prachanda signed on August 9 set forth a strong role for the UN. In addition to requesting the UN to continue its work monitoring human rights in Nepal (Note: the UN's human rights office here is the largest in the world), the letters requested that the UN also assist in monitoring the cease-fire Code of Conduct, monitor Maoist combatants and their weapons, monitor the Nepal Army in its barracks, and supervise and monitor Constituent Assembly elections (which could come by April 2007). What the letter did not do was indicate whether the combatants would be separated from their arms. Most in the SPA agree that Maoists cannot join an interim government until they are separated from their weapons. The GON hopes that the UN will be able to convince the Maoists to agree to such a move.

¶7. Meanwhile, the Nepali authorities and journalists continue to receive reports of Maoist extortion, kidnappings, and other violations of the May 26 Code of Conduct. There are even periodic news reports that the Maoists might initiate another people's movement if they are not admitted soon into an interim government.

ECONOMIC WOES

¶8. Nepal's GDP grew only 1.9 percent in FY 2005/06, while inflation increased to 8 percent annually. Approximately USD 1 billion in foreign remittances pumped into the economy last year increased per capita income to USD 322, a nominal growth of USD 20. The GON, sapped by the Maoist insurgency and

faced with nurturing a fledgling democracy, lacks sufficient financial resources to kick-start economic activity. On July 12, Finance Minister Ram Sharan Mahat announced an ambitious USD 1.97 billion budget for FY 2006/07, which he said was aimed at institutionalizing the democratic system and establishing peace through constituent assembly elections. The budget included USD 325 million in foreign grants, a 72 percent increase over the previous year. Whether the GON will be able to implement the budget hinges on how the peace process unfolds. Final commitments from many donors depend on the GON and Maoists reaching an internationally accepted peace.

¶9. Political turmoil and the Maoist threat have created a hostile business environment. Foreign direct investment has decreased nearly 50 percent since 2000. Nepal is primarily a subsistence agriculture economy, but its industrial base has provided employment to the growing number of poor flocking to the cities. If Nepalese businessmen flee the country instead of trying to work within the current unstable situation, the Nepalese economy will suffer and further hurt the poorest of the poor.

TIBETAN AND BHUTANESE REFUGEES

¶10. Nepal hosts two refugee populations of note, Tibetan and Bhutanese. The USG is currently funding an expansion of the Tibetan Relocation Center located in Kathmandu to make it possible to provide shelter to transiting Tibetans as they wait for processing by UNHCR here in Kathmandu.

¶11. Over 100,000 Bhutanese refugees have been living in seven camps in southeastern Nepal since the early 1990s. Donor countries continue to discuss with the GON options for a durable solution to the Bhutanese refugee issue, including repatriation, local integration, or resettlement of Bhutanese refugees. The GON recently agreed to allow UNHCR to conduct a re-registration of the camps, a necessary step to lay the foundation for future solutions.

A Half-Century Of Development Assistance And Today's USAID Program For Nepal

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¶12. In 1951, the closed Hindu Kingdom of Nepal opened to the outside world. Shortly thereafter, the USG sent our first development assistance to Nepal. The relationship has prospered since, with the United States consistently one of the leading donors in Nepal. Historically, economic assistance through USAID addressed Nepal's poverty and its manifestations, prioritizing health programs, agriculture and natural resources, and other social sector assistance with major success. For example, the rate of child (under five) mortality has dropped by over 40 percent in the 15 years since USAID introduced community-based child health care modalities. USAID was also responsible for the formation of community forest user groups (CFUGS) that have enabled Nepalis to take charge of their major resource and materially slowed deforestation. The CFUGS (over 1700 nationwide) have weathered the storms of civil war and remain an important factor in local self-governance. After the initial advent of democracy in the early 1990s, USAID stepped up assistance with parliamentary training programs. USAID also developed innovative HIV/AIDS activities that have helped to hold the epidemic to the rate of one-half of one percent in the general population despite higher rates in particularly at-risk groups.

¶13. Intensification of the Maoist threat from 2000 on caused the US Mission to reassess the nature of Nepal's problems. USAID introduced strong program elements to mitigate the effects of the conflict and to focus on governance issues such as political party development and the rule of law. The

popular uprising of April 2006, has created new opportunities that Post is eager to grasp. USAID is transitioning into a new strategy for Nepal that targets the goals of stability and security, a multi-sectoral approach which aligns projects to advance the peace process, restore the rural economy shattered by war and terror, and prevent the now-contained HIV/AIDS plague from invading the general population through migrants fleeing the conflict. At the same time, this strategy seeks to bolster the legitimate forces of the central government, empowering GON institutions to rule well, combat corruption, and provide the social services that the rising voice of the population justly demands.

¶14. The USAID program for 2006 has an overall level of approximately USD 45 million, including the core USAID mission programs, new activities by the Office of Transition Initiatives (OTI), and a regional Office of Foreign Disaster Assistance (OFDA) program. About USD 40 million will finance USAID's three strategic objectives for Nepal: A) enhance stability and security, B) strengthen governance and protect human rights, and C) build capacity of critical institutions.

The lion's share of the program budget goes to enhancing stability and security, including components to support the peace process, offer workforce training for unemployed youth, the disadvantaged and the displaced, mitigate conflict and aid victims of conflict, protect the livelihoods of the poor, restore war torn infrastructure through projects such as road-building, and reduce the transmission and impact of HIV/AIDS with its potentially destabilizing effects.

¶15. To strengthen governance and protect human rights, USAID supports activities to reduce trafficking in persons, strengthen civil society and democratic political parties, and support UN and GON efforts to protect human rights. USD 13 million has been allotted to improve critical governmental institutions, including the agencies and local networks that address child survival, health, and nutrition; maternal care; family planning; and the courts and civil society organizations that advance the rule of law and combat corruption. Most recently USG assistance has been augmented by a new program through USAID/OTI that will assist the peace process through media outreach. Lastly, USAID hosts a regional OFDA unit that has, over the past year alone, responded to the Tsunami, the Pakistan earthquake, and even seconded staff for the Katrina response.

MILITARY AND SECURITY ASSISTANCE

¶16. Ensuring law and order is a key responsibility for every government. We look forward to discussing these issues with you in more detail on your arrival.

CONCLUSION

¶17. Let me add in conclusion how delighted I am that you and

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the rest of your delegation, including Rep. Fred Upton and his spouse Amey, Rep. Brian Baird, Rep. Ander Crenshaw and his spouse Kitty, Rep. Wayne Gilchrist, and their staffs, will be coming to Kathmandu. We look forward to welcoming you to Nepal and trust you will find your time here well spent.

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